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Supreme Court of the United States

OCTOBER TERM, 1982

LOCAL 408, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA,

Petitioner,

vs.

NATIONAL LABOR RELATIONS BOARD and BILDISCO and BILDISCO, DEBTORS IN POSSESSION,

Respondents.

PETITION OF LOCAL UNION NO. 408, I.B.T., FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Questions Presented

1. Did the Court of Appeals err in holding that a debtor in possession of a reorganized business may obtain rejection of a collective bargaining agreement under 11 U.S.C. §365(a) of the Bankruptcy Code without requiring that the debtor in possession first comply with the bargaining requirement for mid-term contract modification contained in 29 U.S.C. §158(d) of the National Labor Relations Act prior to obtaining rejection under the Code?

2. Did the Court of Appeals err in ruling that a debtor in possession, who petitions for rejection of a collective bargaining agreement eight months after the debtor had filed for bankruptcy, is a new juridical entity which is not bound by the debtor's labor contract and not bound by the requirements of the labor laws during the period prior to obtaining rejection, even where, as here, all of the workers employed by the debtor in possession in the relevant unit had been employed by the debtor company and were covered by the collective bargaining agreement in effect between the debtor company and the Union?

3. Did the Court of Appeals err in ruling that a petition to reject a labor contract under 11 U.S.C. §365(a) of the Bankruptcy Code may be granted merely after a weighing of the equities even where rejection is not necessary for the continued operation of the company and where the standard used by this Court of Appeals directly conflicts with the more stringent test established by the Second Circuit and followed by the lower courts?

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NO.

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OCTOBER TERM, 1982

LOCAL 408, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA,

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NATIONAL LABOR RELATIONS BOARD and BILDISCO and BILDISCO, DEBTORS IN POSSESSION,

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PETITION OF LOCAL UNION NO. 408, I.B.T., FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Opinions Below

The opinion for the Court of Appeals for the Third Circuit, entered on June 17, 1982, is reported at 682 F.2d 72 (3d Cir. 1982) and is appended to this petition (1a to 25a). The opinion of the District Court for the District of New Jersey was rendered on May 6, 1981, is unreported, and is appended to this petition (28a to 34a). The decision of the Bankruptcy Court was rendered on January 5, 1981, and is unreported.

Jurisdiction

Jurisdiction of this Court is conferred by 28 U.S.C. §1254 (1); that of the Court of Appeals by 28 U.S.C. §1291; that of the District Court by 28 U.S.C. §1334; and that of the Bankruptcy Court by 28 U.S.C. §1471.

Statutes Involved

The statutory provisions involved are the National Labor Relations Act, 29 U.S.C. §151-169 (1976), in particular 29 U.S.C. §158(d), and the Bankruptcy Code, 11 U.S.C. §365 (a).

Statement of the Case

By this petition the petitioner, Local Union No. 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America, seeks the Court's review of a decision of the Court of Appeals for the Third Circuit which vacated the decision rendered by the District Court and remanded the matter to the District Court for further proceedings in conformity with the opinion of the Court of Appeals.* The petitioner does not contest or

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* It should be noted that this case (Court of Appeals No. 81-2140), involving an appeal from decisions below of the Bankruptcy, District and Circuit Courts arising out of the rejection of a labor contract, was consolidated in the Court of Appeals with an enforcement proceeding brought by the National Labor Relations Board

(Footnote continued on following page)

complain of the Court of Appeals' determination of facts in the bankruptcy case or of its reversal and remand of the bankruptcy case. Rather, the petitioner submits that the Court of Appeals erred substantially in its legal analysis and legal conclusions and in the standard of law it instructed the lower courts to apply on remand.

This petition arises out of a motion made in December 1980 by respondent Bildisco, Debtor in Possession, pursuant to 11 U.S.C. §365(a), to reject a collective bargaining agreement signed by Bildisco and the petitioner. Bildisco is a New Jersey partnership engaged in selling and distributing building supplies. Bildisco and the petitioner had been party to a series of collective bargaining agreements, the most recent of which was effective from May 1, 1979 to April 30, 1982. Bildisco was not a party to any other labor contracts. Bildisco had at one time employed 18 persons in the unit covered by the collective bargaining agreement in effect with the petitioner Union. This number decreased to 3 employees by the date of the petition to reject the collective bargaining agreement. All of the workers employed by the Debtor in Possession in the relevant work unit had been employees of the debtor company in that unit and had been covered by the collective bargaining agreement at issue. Several of the Union employees terminated by Bildisco and the Debtor in Possession had nearly 20 years of service to the company.

Commencing in January 1980 Bildisco ceased making pension and welfare payments to the applicable trust funds on behalf of the employees covered by the collective bargaining agreement and also failed to forward to the Union the dues the company was withholding from the employees'

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(Court of Appeals No. 81-2238). The Board and this Union intervened in each other's cases. The Board is also petitioning for a writ of certiorari. For purposes of clarity, where needed, the Board's case will be referred to as the "enforcement" case and the Union's case will be referred to as the "bankruptcy" case.

pay checks. On April 14, 1980 Bildisco filed for bankruptcy under Chapter 11 of the Bankruptcy Code. The bankruptcy court appointed the partnership as Debtor In Possession and authorized it to operate the business under 11 U.S.C. §1107. Bildisco, Debtor In Possession, continued to fail to make pension and welfare payments and to fail to forward to the Union the dues it deducted from the employees' pay checks. The Debtor In Possession also failed to give the employees the raises as called for by the collective bargaining agreement and denied them vacation pay. At no time did the debtor company or the Debtor In Possession seek to negotiate with the Union concerning changes in the collective bargaining agreement.

In December 1980 the Debtor In Possession petitioned the Bankruptcy Court under 11 U.S.C. §365(a) for rejection of the collective bargaining agreement. A hearing was held on January 5, 1981, after which the Bankruptcy Court approved the petition to reject the labor contract. The Bankruptcy Court did not explain what standard it was using in approving rejection.

The Union appealed this decision to the District Court. The District Judge observed that under the superseded Bankruptcy Act judicial evaluations of petitions to reject contracts utilized a "business judgment" test for normal contracts and a more rigorous test for labor contracts (30a to 31a). Accepting without comment the figures found by the Bankruptcy Court, the District Court ruled that the contract would have been rejected under either standard and it was therefore not necessary to determine which standard should apply. Accordingly, the District Court affirmed the Bankruptcy Court decision approving rejection of the collective bargaining agreement in effect between Bildisco and the petitioner without deciding what standard of law applies.

The petitioner then appealed to the Third Circuit. Noting that the appeal presented "a significant confrontation of labor and bankruptcy policies", the Third Circuit viewed its task as reconciling the apparent conflict between the

National Labor Relations Act (NLRA) and the Bankruptcy Code (Code) (10a, 7a).

Despite the existence in the NLRA of provisions dealing expressly with mid-term modification of labor contracts (29 U.S.C. §158(d)), the Third Circuit commenced and centered its reconciliation upon the Code. The court first examined whether the Code expressly excluded labor contracts from its purview (70a to 11a). Though acknowledging that no clear congressional intent in this area could be discerned, the court found several factors leading it to view NLRA contracts as within the scope of the Code. To this end the Third Circuit noted that prior to the enactment of the new Code there were several court decisions allowing rejection of a collective bargaining agreement under the bankruptcy laws; that the Code specifically exempted certain other types of contracts (such as shopping center leases); and that there was an exception in the Code (11 U.S.C. §1167) for labor contracts under the Railway Labor Act (RLA). The court concluded not only that NLRA contracts are covered by the rejection provision in the Code, but also expressly ruled that there is no requirement to comply with §8(d) of the NLRA prior to rejection under the Code (12a, 21a).

The court then turned to an analysis of the applicable standard which a court should employ in determining whether to approve rejection of NLRA contracts under §365(a). The court noted that the standard for rejecting normal contracts is the "business judgment" test, whereby a contract may be rejected if the debtor in possession demonstrates that a more beneficial contract can be entered into (12a). The court also observed that under the superseded Bankruptcy Act the courts had established a more stringent test for rejection of labor contracts (12a). As the Third Circuit observed, this stricter test was first announced by a circuit court in *Local Union No. 455* v. *Kevin Steel Products Inc.*, 519 F.2d 698, 707 (2d Cir. 1975), in which the Second Circuit stated that a rejection of a labor contract may occur after a "thorough scrutiny, and a careful balancing of the equities on both

sides." As the Third Circuit further noted, the Second Circuit subsequently expanded upon that standard by ruling that a labor contract may be rejected only where the debtor in possession shows both that rejection is necessary to save the debtor company from imminent collapse and that a balancing of the equities weighs in favor of the debtor. *BRAC* v. *REA Express, Inc.*, 523 F.2d 164, 169, 172 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1975) (13a). The Third Circuit obliquely observed that the lower courts have followed the test as enunciated in *REA Express* (13a to 14a).

However, the Third Circuit expressly rejected the Second Circuit's test as stated in *REA Express*, castigating it as mere "gloss" upon, and the "illegitimate progeny" of, *Kevin Steel* (13a; 16a). Instead, the Third Circuit declared that a labor contract may be rejected after a "thorough scrutiny, and a careful balancing of the equities on both sides." (A15). Because the District and Bankruptcy Courts below had approved rejection of the labor contract without clearly stating the standard or the elements of the balancing, the decision below was reversed and the matter was remanded for further proceedings consistent with the Third Circuit's opinion.

In seeking this Court's review by writ of certiorari the petitioner does not dispute the Third Circuit's factual assessments or its reversal and remand of the bankruptcy case. The petitioner requests review because of the erroneous legal reasoning and ruling rendered by the Court of Appeals. Nor, significantly, does the petitioner dispute the Third Circuit's conclusion that NLRA labor contracts are executory contracts which may ultimately be reviewed and rejected under §365(a) of the Code. Rather, the petitioner's disagreement with the Third Circuit is twofold. First, the petitioner submits that the Third Circuit wrongly ignored the provisions and policies of the NLRA by holding that rejection under the Code could be granted without first requiring the debtor company or debtor in possession to have complied with the mid-term concession bargain-

ing requirement contained in §8(d) of the NLRA. Secondly, the Third Circuit erred—and created a substantial and direct conflict between the circuits—in ruling that a labor contract could be rejected simply after a weighing of the equities and without consideration of whether rejection is necessary to the continued operation of the company.

As noted above, this case is part of a consolidation of two cases presented to and decided by the Third Circuit. The sibling case is an enforcement petition filed by the National Labor Relations Board arising out of unfair labor practice complaints concerning the conduct of the company before it filed for bankruptcy in April 1980 and during the period between the April 14, 1980 filing and the January 1981 rejection of the contract. In those complaints the Board alleged that the company's pre and post-filing unilateral changes in the terms and conditions of employment violated the NLRA. Because the debtor in possession failed to respond to the complaints, summary judgment against it was rendered by the Board.

However, the Third Circuit concluded that, under the facts of this case, entry of summary judgment was improper (22a to 24a). Secondly, the court ruled that the debtor in possession was a new entity, not bound by §8(d) or by the collective bargaining agreement in effect between the debtor and the petitioner union (20a to 21a). Accordingly, the Third Circuit refused to enforce the Board's order.

The Board is petitioning this Court on the issues flowing from the Third Circuit's ruling that the debtor in possession is a new entity not bound by the contract of the debtor company or by §8(d). Consequently, the petitioner will not burden the Court with lengthy argument on that matter. This petitioner supports the arguments made by the Board in its petition.

ARGUMENT

POINT I

The decision of the Court of Appeals that a debtor in possession may reject a labor contract under 11 U.S.C. §365(a) of the Bankruptcy Code without requiring that the debtor in possession first comply with the bargaining requirement for mid-term contract modifications contained in 29 U.S.C. §158(d) of the National Labor Relations Act should be reviewed by this Court because it presents a significant issue of reconciling a conflict between two fundamental statutory schemes and because the Court of Appeals' decision constitutes an improper analysis and treatment of these two statutes.

This petition presents the Supreme Court with a conflict between two comprehensive statutory schemes: the National Labor Relations Act, 29 U.S.C. §§151-169 (1976), which defines the rights of workers and the method of making, maintaining, and modifying labor contracts, and the Bankruptcy Code, 11 U.S.C. §§101-1330 (1979), which permits a financially distressed business to rearrange its operation, restructure its debt, and reject its executory contracts. The conflict arises when a debtor in possession seeks to terminate a collective bargaining agreement which the debtor had signed with a union. Though this issue clearly implicates both the letter and spirit of the labor law, the Court of Appeals for the Third Circuit resolved the conflict by holding that the provisions of the NLRA are wholly inapplicable and by formulating a standard for rejection of labor contracts under the Bankruptcy Code which disserves the labor law and needlessly destroys the pension and seniority rights earned by the workers. Furthermore, in creating this standard the Third Circuit explicitly eschewed as "illegitimate" the test previously enunciated by the Second Circuit and followed by the lower courts throughout the nation under the superseded Bankruptcy Act and the new Code.

Resolution of this tension between the labor and bankruptcy laws, and of the now existing direct conflict between the Second and Third Circuits, is of national import, for what is at stake here is not the technical question of statutory construction but whether the pension, welfare and seniority rights earned by this country's workers must be sacrificed to the sanctity of a bankruptcy plan where the sacrifice is not essential to the continued operation of the company. Resolution of this question is made all the more imperative because of the increasing number of bankruptcies being filed by businesses.* Clearly the conflict between the circuits on this issue is a matter of great public concern requiring resolution by the highest forum.

The petitioner's position on the reconciliation of these two statutory schemes, and on the Third Circuit's errors, is both simple and equitable: a debtor in possession must attempt to modify its labor contract in compliance with the express provisions of the NLRA (29 U.S.C. §158 (d)) before obtaining rejection of that labor contract under the Bankruptcy Code (11 U.S.C. §365(a)).** Only after the

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* Commentaries on the large number of bankruptcies filed during the past year have been widely reported in the press. For example, in the first of a four-part article reported in the New York Times, it was stated that, during the year ending June 30, 1982, 77,503 businesses filed for bankruptcy in the federal courts. N.Y. Times, Sept. 30, 1982, at page 1, col. 2.

** 29 U.S.C. §158(d) provides in pertinent part that:

> (d) For the purposes of this section, to bargain collectively is the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment, or the negotiation of an agreement, or any question arising thereunder, and the execution of a written contract incorporating any agreement reached if requested by either party, but such obligation does not compel either party

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bargaining required by §8(d) has failed should the debtor in possession be able to obtain rejection of a labor contract under §365(a) of the Code. The Third Circuit's errors consist of: (a) its exclusion of any role for the labor laws

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to agree to a proposal or require the making of a concession: *Provided,* That where there is in effect a collective-bargaining contract covering employees in an industry affecting commerce, the duty to bargain collectively shall also mean that no party to such contract shall terminate or modify such contract, unless the party desiring such termination or modification—

(1) serves a written notice upon the other party to the contract of the proposed termination or modification sixty days prior to the expiration date thereof, or in the event such contract contains no expiration date, sixty days prior to the time it is proposed to make such termination or modification;

(2) offers to meet and confer with the other party for the purpose of negotiating a new contract or a contract containing the proposed modifications;

(3) notifies the Federal Mediation and Conciliation Service within thirty days after such notice of the existence of a dispute, and simultaneously therewith notifies any State or Territorial agency established to mediate and conciliate disputes within the State or Territory where the dispute occurred, provided no agreement has been reached by that time; and

(4) continues in full force and effect, without resorting to strike or lock-out, all the terms and conditions of the existing contract for a period of sixty days after such notice is given or until the expiration date of such contract, whichever occurs later:

11 U.S.C. §365(a) of the new Bankruptcy Code provides:

"Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."

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prior to rejection of a labor contract,* and (b) its formulation of a standard for allowing rejection of a labor contract under §365(a) of the Code which contravenes the purposes of the labor laws, conflicts with the standard devised by the Second Circuit, and allows the destruction of pension, welfare and seniority rights even where it is not necessary for the continued operation of the reorganized business.

It is at this point an elementary lesson in history that the industrialization of this nation was marred by the economic warfare flowing from the effort of factory work-

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Significantly, an "employer" for purposes of the NLRA includes trustees in chapter 11. 29 U.S.C. §152(1), (2). Also, it is at this point axiomatic that the requirement in 29 U.S.C. §158 (d) (also called §8(d)) for bargaining applies to any effort by a party to a labor contract to effect a mid-term change in the contract. *Dunham-Bush, Inc.*, 111 L.R.R.M. (BNA) 1389, 1391, 264 N.L.R.B. No. 175 (1982); *Oak Cliff-Golman Baking Co.*, 85 L.R.R.M. (BNA) 1035, 1036, 207 N.L.R.B. 1063, 1064 (1973), enfd, 505 F.2d 1302 (5th Cir. 1974); *C & S Industries, Inc.*, 62 L.R.R.M. 1043, 158 N.L.R.B. 454, 459 (1966). These cases also make clear that a violation of §8(d) constitutes an unfair labor practice in contravention of 29 U.S.C. §158(a)(5).

* In its brief below this petitioner did not explicitly argue that §8(d) must be followed prior to obtaining rejection under §365(a) of the Code. However, that argument was clearly at issue in the Board's enforcement case, in which the petitioner intervened and supported the Board. Moreover, the Third Circuit's decision expressly states and holds that there is no need to comply with §8(d) before obtaining rejection under the Code (12a, 21a). The Third Circuit premised that conclusion upon its "new entity" theory, which was clearly in issue below. Also, the petitioner's arguments concerning the need to adhere to §8(d) prior to resort to §365(a) is a purely legal argument which is entirely consistent with its argument below. For these reasons, the question concerning the role of §8(d) of the NLRA in relation to §365(a) of the Code is properly before, and reviewable by, this Court. *Kiefer-Stewart Company* v. *Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211, 214 (1951).

ers to unite so as to obtain reasonable wages and humane working conditions. That warfare led to the enactment of the NLRA. The NLRA embodies the carefully conceived congressional arrangement of the balance of economic power appropriate between labor and management and it prescribes procedures which promote and maintain that economic equivalence. The balance struck by Congress is a matter of public policy and is not to be restructured by the judiciary. *Teamster Union Local 20* v. *Morton*, 377 U.S. 252, 259 (1964).

Indeed, the courts have been respectful of the elaborate system of laws establishing and regulating labor relations. In particular, the courts have long noted the embattled origin and unique nature of labor contracts. As this Court explained:

> "The collective bargaining agreement states the rights and duties of the parties. It is more than a contract; it is a generalized code to govern a myriad of cases which the draftsmen cannot wholly anticipate . . . The collective agreement covers the whole employment relationship. It calls into being a new common law—the common law of a particular industry or of a particular plant . . .
> . . . A collective bargaining agreement is an effort to erect a system of industrial self-government. When most parties enter into contractual relationship they do so voluntarily, in the sense that there is no real compulsion to deal with one another, as opposed to dealing with other parties. This is not true of the labor agreement. The choice is generally not between entering or refusing to enter into a relationship, for that in all probability preexists the negotiations. Rather it is between having that relationship governed by an agree-upon rule of law or leaving each and every matter subject to temporary resolution dependent solely upon the relative strength, at any given amount of the contending forces."

United Steelworkers v. *Warrior & Gulf Nav. Co.*, 363 U.S. 574, 578-579 (1960).

The rights created and affected by a labor contract are two-fold: the rules which maintain order at the workplace and the rules which guarantee economic security to the workers. Among the former are seniority, grievance-arbitration procedures for dispute resolution, disciplinary procedures, and no-strike/no lock-out clauses. Among the latter are welfare and pension plans. Unlike a normal commercial contract, a collective bargaining agreement is an organic being whose terms are gleaned not merely from its express clauses but also from the history of relations between the workers and the company. *John Wiley & Sons* v. *Livingston*, 376 U.S. 543, 550 (1963). Furthermore, the rights and benefits earned by the workers are not measured by the existence of any one contract; rather, those rights and benefits derive their value from the expectation that the parties will continue to sign and adhere to successive labor contracts guaranteeing the pension and seniority rights accrued during any single contract. This expectation of successive contracts is predicated upon the core factor which distinguishes the specie "labor" contract from its genus of "executory" contract: workers and management cannot exist without each other, thereby rendering the notion of "voluntariness" irrelevant. Moreover, the rights and benefits accrued over time by the workers cannot be remedied by the usual means of awarding damages. For example, unlike the normal commercial contract freely entered into by business adventurers, the pension and seniority rights earned by the workers defy adequate compensation if the employer is allowed to simply end the contract. See 11 U.S.C. §507(a)(3)(4). See also *Local No. 455* v. *Kevin Steel, supra* at 707.*

* Importantly, the petitioner is not suggesting that labor contracts fall outside the category of executory contract. The petitioner acknowledges that, ultimately, a labor contract may be subject to rejection under §365(a) of the Code. The petitioner's argument is simply that a labor contract is a unique specie and, because it is completely defined and determined by the NLRA, resort should be had to that statute prior to rejection review under §365(a).

The policies and purposes of the Bankruptcy Code are entirely different. That Code serves two primary functions: to preserve funds for distribution to creditors and to allow a faltering company to facilitate financial rehabilitation through reorganization rather than liquidation. *Meyer* v. *Commissioner*, 383 F. 2d 883, 890 (8th Cir. 1967). A reorganized company continues in operation, a trustee or debtor in possession is appointed by the court to manage the company during its recovery, and its debts are reduced or extended so as to allow it to continue. As is the case here, the court will often appoint the owners of the debtor company to continue to operate the reorganized business as "debtor in possession." As here, the debtor in possession may be employing the same workers in the same jobs and for the same managers as the prebankrupt company.* As part of the reorganized company's effort to devise economic arrangements conducive to its continuance, the Code provides that the debtor in possession may petition the court to reject an executory contract. 11 U.S.C. §365(a).

As described above, §8(d) of the NLRA explicitly contains an absolute requirement that a party seeking to effect mid-term changes in its labor contract so as to obtain more beneficial terms may do so only if it bargains with and obtains the consent of the other party. See *C & S Industries, Inc., supra*, 62 L.R.R.M. at 1045. Though the party being requested to agree to changes is not required to negotiate, no less consent to any changes, §8(d) at least creates the mechanism for and possibility of arriving at mid-term modifications without resort to strikes, lock-outs, or unfair unilateral changes in the contract. Contrary to the mid-term modification procedures in §8(d) formulated by Congress to deal exclusively with labor contracts, contract rejection in §365(a) of the Code is merely a general grant of power

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* It should be emphasized that the issues in this case deal only with a company in reorganization, not with one in liquidation.

to a court to approve rejection of "executory contracts" or "unexpired leases." Section 365(a) does not define executory contract, does not refer or allude to labor contracts, and does not contain any mechanism or authority for modifying a contract. 2 Collier on Bankruptcy ¶365.01[2], at 365-11 (15th ed. 1981).

Viewed against this background, the question of how and when a debtor in possession may modify or terminate it labor contract may now be answered. A fundamental rule of construction is that "a more specific statute will be given precedence over the more general one, regardless of their temporarl sequence." *Busic* v. *United States,* 446 U.S. 398, 406 (1980). See also *Preiser* v. *Rodriguez*, 411 U.S. 475, 489-490 (1973). Addressing an essentially identical statutory relationship, this Court instructed that where one statute pertains to a particular subject and contains a provision applying to a specific situation, that statute must control over a more broad statute which may also cover in its generality the same situation. *Morton* v. *Mancari,* 417 U.S. 535, 550-551 (1974). At the very least, where two laws may apply to the same problem and are capable of co-existence, a court should not ignore one. *Morton* v. *Mancari, supra.* Based upon these precepts of statutory construction and reconciliation, it is manifestly evident that the more apposite provisions in §8(d) of the NLRA, which is an essential aspect of a comprehensive statutory scheme regulating the precise specie of contract at issue here, should be given priority over the more general and undefined provision of the Code covering rejection of the genus of executory contracts.

Another factor which supports the priority of the NLRA is the capacity of that statutory process to allow for the preservation of essential worker rights and benefits while simultaneously serving the debtor's need to reduce expenses. Section 8(d) of the NLRA allows for modification of collective bargaining agreements without interrupting the production of goods. *Mastro Plastics Corp.*

v. *NLRB*, 350 U.S. 270, 284 (1956). Section 8(d) provides the authority and basis for the parties to a labor agreement to at least seek a modification of the labor contract because of the new needs or problems of one party. During this process the debtor company would undoubtedly be able to impress upon the union the distressed state of the company's finances, compellingly evidenced by its having filed for bankruptcy. In light of the desire of the union to save jobs and pensions, the parties would hopefully bargain and agree upon a modified contract which would both substantially reduce the company's expenses and preserve essential worker rights. For example, the union may agree to forgo raises, give back some holidays and break-time, and shorten the hours worked by each employee, thereby preserving seniority rights and pension and welfare payments, and maintaining the grievance and arbitration procedures.*

The range of possible compromises is limited solely by the parties' imaginations. If they are unable to agree upon modifications, or if the union refuses to negotiate, then—but only then—should the employer be able to obtain rejection of the contract under §365(a) of the Code. However, it is only by following the procedures in §8(d) of the NLRA that the parties can even attempt to devise a mutually satisfactory mid-term modification.

Unlike §8(d) of the NLRA, §365(a) of the Bankruptcy Code does not provide for or permit mere modification. Rather, it is an all or nothing proposition and a court cannot fashion a compromise. *In re David A. Rosnow, Inc.*, 9 Bankr. Rpts. 190, 193 n. (Bankr. D. Conn. 1981);

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* The labor reports are replete with discussions of successfully negotiated "give back" or "concession" contracts in which the unions forgo wage and cost of living increases, surrender days of pay or agree to invest that pay in the company, and agree to decreases in break-time in exchange for job protections and assurances against plant closings. See, *e.g.* 109 L.R.R.M. (BNA) 213, 214, 228, 229, 321 (1982); 110 L.R.R.M. (BNA) 3, 83 (1982).

2 Collier on Bankruptcy, ¶365.01[2] at 365-11 (15th ed. 1981). To be sure, the debtor in possession who obtains rejection of a labor contract under §365(a) may be obliged to negotiate a new contract with its employees should they still desire a union's representation, *Local Union No. 455* v. *Kevin Steel, supra* at 704, but clearly the ability of the workers to retain their basic economic and seniority related benefits is reduced where the contract has already been terminated. Moreover, under the Third Circuit's theory that a debtor in possesesion is a new legal entity akin to a successor, the debtor in possession may not be under any obligation to even bargain with the workers. *Howard Johnson Co.* v. *Hotel Employees,* 417 U.S. 249, 259-262 (1974). *NLRB* v. *Burns International Security Services,* 406 U.S. 272 (1972). Even if the debtor in possession is obliged to bargain because a majority of its relevant workforce had been employed by the debtor, bargaining prior to termination prevents a disruption in the accrual of seniority and pension rights and lessens the likelihood of a crippling strike which an employer's unilateral changes would induce.

Plainly stated, Congress has carefully composed a body of rules and procedures regulating the formation, alteration, and termination of labor contracts. That statutory scheme allows for relief where one side's economic position has so drastically changed as to necessitate modification. An administrative agency has been vested with authority to monitor labor contract changes so as to maintain industrial peace, preserve the continued operation of the employer, and safeguard the employees' basic rights. While the bankruptcy laws do contain a provision generally allowing for the total rejection of an "executory contract," that provision should not take precedence over the more apposite labor laws. The NLRA, and its enforcement agency, should be afforded initial supervision over the modification of a labor contract. "[W]here the matter in controversy has been entrusted by Congress to an administrative agency, the bankruptcy court normally should stay

its hand . . ." *Nathanson* v. *NLRB*, 344 U.S. 25, 30 (1952). That principle should pertain here.

Contrary to the well established principles of statutory construction which accord precedence to specific statutes over general ones, and contrary to this Court's admonition that labor issues should be monitored by the agency charged by Congress with responsibility for enforcement of labor laws rather than by a bankruptcy court, the Third Circuit eschewed the notion that the labor laws even apply to an attempt to reject a labor contract (12a, 21a). Instead, the Third Circuit stood these interpretative rules on their head and reasoned that because §365(a) of the Bankruptcy Code does not declare that labor contracts are immune from rejection, they are exclusively and solely within the purview of §365(a). This inverse approach to statutory acommodations must be reversed.

A clue to the Third Circuit's backwards approach to statutory construction and conciliation may be found in its reference to two notions: 1) the provision in the Code which exempts from §365 those labor contracts which are subject to the Railway Labor Act, and 2) the description of the debtor in possession as a "successor." However, neither notion supports the Third Circuit's preclusion of the applicability of the NLRA prior to rejection review under the Code.

To be sure, the Code does contain a proviso which exempts RLA labor contracts from review under §365. 11 U.S.C. §1167.* But this exception does not suggest the inference that NLRA contracts may not initially be subjected to the requirements of §8(d) of the NLRA before such contracts are evaluated for rejection under §365(a) of the

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* 11 U.S.C. §1167 states:

> "Notwithstanding section 365 of this title, neither the court nor the trustee may change the wages or working conditions of employees of the debtor established by a collective bargaining agreement that is subject to the Railway Labor Act (45 U.S.C. 151 et seq.) except in accordance with section 6 of such Act (45 U.S.C. 156)."

Code. Indeed, little can be gleaned from the RLA exception in §1167.* Section 1167 was contained in the superseded Bankruptcy Act in 11 U.S.C. §205(n) (also known as §77(n)). That section was enacted in 1934, after the RLA but before the passage of the NLRA. (Section 8(d) was added to the NLRA in 1947.) Obviously, the failure of §205 (n) to include NLRA contracts cannot be laid to congressional intent. See *Local Union No. 455* v. *Kevin Steel Products, Inc.*, 381 F. Supp. 336, 338 (S.D. N.Y. 1974), *reversed*, 519 F.2d 698 (2d Cir. 1975) That NLRA contracts were not incorporated into §1167 in the 1978 revision of the bankruptcy laws is at best a speculative basis upon which to conclude that NLRA labor contracts are completely stripped of their unique nature, thereby excluding any role for the NLRA. On the contrary, the legislative history of §205(n), the progenitor of §1167, reveals that the RLA exception was predicated upon principles equally appropriate to NLRA contracts: to protect workers from the unilateral action of bankrupt employers reducing wages and benefits. 76 Cong. Rec. 2927 (1933). See also Note, *Bankruptcy And The Rejection of Collective Bargaining Agreements*, 51 Notre Dame Lawyer 819, 827 (1976). Simply stated, the RLA exception contained in §1167 does not suggest or require the conclusion that NLRA labor contracts cannot or should not be subjected to the

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* Judicial interpretation of the scope of §1167 is sorely muddled. In *Local 455* v. *Kevin Steel, supra* at 705, the Second Circuit, acknowledging that Congress' silence on NLRA contracts is capable of various inferences, concluded that the RLA exception applied only to "labor contracts" covered by the RLA. However, upon reexamination the Second Circuit determined that the exception applied only to "railroad employees," not to "contracts." *BRAC* v. *REA Express, Inc., supra* at 170. Thus the present status of the RLA exception is based not on whether the contract is subject to the RLA or the NLRA but on whether the affected employees are railroad or non-railroad employees—an analysis which has no bearing on whether NLRA contracts may not be subjected to the provisions of §8(d) of the NLRA prior to rejection review under §365(a) of the Code.

bargaining provisions of §8(d) of the NLRA before being evaluated under §365(a) of the Code.

Also mistaken is the Third Circuit's use of the successor analogy. Under this theory, first set forth by the Second Circuit in *Kevin Steel*, a debtor in possession is likened to a successor as described in *NLRB* v. *Burns International Security Services*, 406 U.S. 272 (1972). According to the Third Circuit, the successor is a "new entity," legally different and apart from the prebankrupt company and thus neither a party to the labor contract the company had signed with the union nor bound by the requirements of §8(d) of the NLRA. This analogy is neither legally supportable nor pragmatically useful.

In reorganizations under the Code the debtor in possession is often, as it is here, the exact same people who owned and operated the pre-bankruptcy company. This is vastly different than a successor who, as in *Burns* and *Howard Johnson*, is an entirely different, unrelated company which purchases the predecessor's operation or which completely replaced the predecessor in supplying a service. While it is eminently reasonable to conclude that a replacement or purchasing company is a wholly different legal entity from the completely separate predecessor, there is no rational basis for viewing the pre-bankruptcy owners as legally different simply because those same persons are now labeled debtors in possession. *Howard Johnson Co.* v. *Hotel Employees, supra* at 259 n.5. Not only is the debtor in possession frequently the same people as those who previously ran the company, the debtor in possession will eventually become the owner of the ongoing post-bankruptcy company. In short, the debtor in possession in a reorganized company is merely a label reflecting the supervisory role played by a bankruptcy court during the period of economic illness from which the company is temporarily suffering.

Furthermore, the theory that a debtor in possession is unfettered by the contracts of the prebankruptcy company is undermined by numerous other circuit court deci-

sions which have bound the debtor in possession to the debtor company's prebankruptcy obligations. For example, in *NLRB* v. *Baldwin Locomotive Works,* 128 F.2d 39 (3d Cir. 1942) the NLRB sought to enforce a remedy against a debtor in possession for unfair labor practices committed in prebankruptcy by the debtor. The debtor in possession defended by arguing that the debtor and debtor in possession were distinct entities and cannot be held responsible for the acts of each other. *NLRB* v. *Baldwin Locomotive, supra* at 42. The court disregarded the alleged separateness and looked instead at the substance of the relationship, concluding that the commonality of interest far outweighed any differences. As the *Baldwin* court explained:

> "[w]here managerial control and economic interest of the debtor in possession and the [debtor] company are the same . . . then in no legally significant sense . . . can the [debtor] be differentiated from the debtor in possession so far as the employer-employee relationship is concerned."

NLRB v. *Baldwin Locomotive, supra* at 43-44.

Similarly, numerous other courts have eschewed the theory underlying the new entity notion. In *NLRB* v. *Coal Creek Coal Company,* 204 F.2d 579, 580 (10th Cir. 1953) the court, citing *Southport Petroleum Company* v. *NLRB,* 315 U.S. 100 (1942), held that liability for prebankruptcy infringements of labor laws cannot be evaded by "reorganization, transfers, or any other 'disguised continuance' ", including receivership. See also *Johnson* v. *England,* 356 F.2d 44, 49 (9th Cir. 1966). In different but equally apposite contexts the circuit courts have ruled that a bankruptcy court's equitable powers are limited by the prohibitions on injunctions contained in the Norris-LaGuardia Act (29 U.S.C. §101 *et seq.*), (See, *e.g., In re Third Avenue Transit Corp.,* 192 F.2d 971, 973 (2d Cir. 1951)), and that the automatic stay provisions of the Bankruptcy Code are subordinate to the requirements of

the labor laws. *Petrusch* v. *Teamster Local 317*, 667 F.2d 297 (2d Cir. 1981); *In re Bel Air Chateau Hospital*, 611 F.2d 1248 (9th Cir. 1979).

It is therefore hardly surprising that the "new entity" doctrine espoused by the Second Circuit in *Kevin Steel* and adopted by the Third Circuit *sub judice* has been criticized by the legal community. As one commentator stated:

> "[I]t is difficult to see how a debtor in possession can be truly distinct from its former self. Where there have been no changes in management, except to introduce overall bankruptcy court supervision, any analogy to successor employer situations seems tenuous."

Note, *Bankruptcy Law—Labor Law—Rejection of Collective Bargaining Agreements As Executory Contracts in Bankruptcy*, 22 Wayne L. rev. 165, 173 (1975). Accord, Countryman, *Executory Contracts in Bankruptcy: Part II*, 58 Minn. L. Rev. 479, 489 (1974); LaPenna, *Bankruptcy and Collective Bargaining Agreement*, 29 N.Y.U. Lab. Conf. 169, 172 (1976). Recently a district court observed that the new entity theory "does not easily translate into other areas of bankruptcy law." *In re Allied Supermarkets, Inc.*, 6 Bankr. Rptr. 968, 976 n. 8 (E.D. Mich. 1980).

Indeed the new entity theory creates paradoxes and problems which would challenge Zeno. For example, if a debtor in possession is a new entity and thus not bound as a matter of law by the prebankruptcy company's labor contracts, then why does the debtor in possession need to petition to reject that contract at all? Similarly, if the debtor in possession is not bound by the labor contract, then surely the language in §365(g) describing rejection as a "breach" of the contract is confusingly inappropriate. Also, if the debtor and debtor in possession are wholly distinct legal beings, is the postbankruptcy company or union bound by a labor contract assumed under §365(a) by the debtor in possession? Perhaps these

problems have contributed to the Second Circuit's continual narrowing of the new entity theory it conjured up in *Kevin Steel.* See *In re Unishops,* 543 F.2d 1017, 1018-1019 (2d Cir. 1976); *Truck Drivers Local 807* v. *Bohack Corp.,* 541 F.2d 312, 319-20 (2d Cir. 1976), *aff'd per curiam after remand,* 567 F.2d 237 (2d Cir. 1977), *cert. den.,* 439 U.S. 825 (1978) (Second Circuit limited the "new entity" theory solely to rejection of labor contracts.). But these abortive and awkward efforts to preserve the untenable "new entity" fiction will not suffice. The increasingly artificial reasoning needed to sustain the life of that wrongfully conceived doctrine must be removed. The more sound and workable position is that the debtor in possession remains bound by the terms of the labor contract and should comply with the negotiation requirement created by Congress in §8(d) of the NLRA for mid-term modification before obtaining rejection under §365(a). The Third Circuit's adoption and use of the new entity theory should be discarded and corrected by this Court.

Before proceeding to the second and final Point in this petition, it must be noted that if the successorship concept were applicable here, the result should have been that Bildisco, Debtor in Possession, was bound by both the labor contract and §8(d) of the NLRA. In *NLRB* v. *Burns International Security Services, supra,* upon which the Third Circuit relied in employing the new entity analysis, the successor company out-bid and replaced the predecessor in providing security services at a facility. The successor ultimately employed 42 guards, 27 of whom had been employed by the predecessor and had been under a collective bargaining agreement. The successor refused to bargain with its employees and the NLRB ordered it to honor the terms of the collective bargaining agreement. The Court found that there was no merger, sale of assets, or dealings between the predecessor and successor; rather, they were entirely separate companies who competed on bids for security servies. *NLRB* v. *Burns, supra,* at 286. Because of the

utter absence of any relationship between the two companies, the Court concluded that the successor was not a party to the collective bargaining agreement in effect between the union and the predecessor and was not obligated to comply with that contract. *NLRB* v. *Burns, supra* at 286-287. However, the Court also ruled that though a successor is ordinarily free from the terms of its predecessor's contract and free to set new initial terms of employment, there would be circumstances under which the successor would be required to consult with the union prior to fixing new terms of employment. *NLRB* v. *Burns, supra* at 294-295. For example, where the successor decided to employ all or most of the workers who had been employed by the predecessor under the collective bargaining agreement, then the successor must bargain with the union before making any changes in the terms of employment. *NLRB* v. *Burns, supra* at 295. In the instant case it was never disputed that all of the Debtor in Possession's employees performing bargaining unit work had been employees of the prebankrupt company and had been covered by the labor contract. Thus, under *Burns,* the Debtor in Possession would have been required to bargain with the petitioner Union prior to instituting changes in the contract.

The Third Circuit's failure to correctly apply the successorship theory only emphasizes its error in employing the analogy in the first place. Moreover, the error is not limited to the question whether a debtor in possession should be required to comply with §8(d) of the NLRA prior to obtaining rejection under §365(a) of the Code; it also implicates the Third Circuit's holding that upon rejection the debtor in possession is immune from unfair labor practice violations arising out of its post-filing conduct. (In this case that would immunize the Debtor in Possession from liability for the unilateral changes it made after April 14, 1980, the date upon which the debtor filed for bankruptcy). The Third Circuit's conclusion that as a matter of law rejection of a labor contract retroactively protects the debtor in possession from violations of the labor laws resulting from his having made unilateral changes in the terms of employment flies in the face of the Supreme Court's holdings in *Burns.*

POINT II

The decision of the Court of Appeals that a labor contract may be rejected under 11 U.S.C. §365(a) of the Bankruptcy Code merely upon a weighing of the equities should be reviewed by this Court because it directly conflicts with the standard developed by the Second Circuit and followed by the lower courts and because the standard adopted *sub judice* is unnecessarily destructive of workers' pension, welfare and seniority rights.

Whether this Court agrees with the petitioner that the bargaining provisions in §8(d) of the NLRA should be employed and exhausted prior to a rejection of a labor contract under §365(a) of the Code, or agrees with the Third Circuit that rejection of a labor contract may proceed under §365(a) without regard to the dictates of the NLRA, it is apparent that the standard established by the Third Circuit for review of labor contracts under §365(a) is woefully inadequate and in direct conflict with the more considered standard formulated by the Second Circuit and followed by the lower courts. It is submitted that whenever a court evaluates a petition under §365(a) to reject a labor contract, the test established by the Second Circuit in *REA Express* should control.

Prior to the Third Circuit's decision in this case, the courts throughout the nation applied the test enunciated in *REA Express* by the Second Circuit for evaluating petitions to reject labor contracts under the Bankruptcy Act.* As noted above, that standard was developed by

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* Petitions to reject executory contracts under the superseded Bankruptcy Act were made pursuant to §313(1), the equivalent of the current §365(a). 11 U.S.C. 313(1) stated, in pertinent part, that:

> "Upon the filing of a petition, the court may, in addition to the jurisdiction, powers, and duties conferred and imposed upon it by this chapter—(1) permit the rejection of executory contracts of the debtor, upon notice to the parties of such contracts and to such other parties as the court may designate[.]"

the Second Circuit in a series of cases. In its first decision on this topic the Second Circuit stated that rejection of a labor contract may be approved "only after a thorough scrutiny, and careful balancing of the equities on both sides . . ." *Local No. 455* v. *Kevin Steel, supra* at 707. This test was plainly more rigorous than the usual "business judgment" test applied to normal executory contracts. The reason for the heightened scrutiny of labor contracts was simple, for in allowing rejection of a labor contract the court

> "may be depriving the employees affected of their seniority, welfare and pension rights, as well as other valuable benefits which are incapable of forming the basis of a provable claim for money damages."

Local No. 455 v. *Kevin Steel, supra* at 707.

Indeed, it was this Draconian consequence of rejection under the bankruptcy laws which compelled the Second Circuit to clarify and reinforce the requirements for approval of a petition to reject a labor contract. *BRAC* v. *REA Express, Inc.*, 523 F.2d 164, 172 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1975). See also, Note, *Bankruptcy Law—Labor Law, Rejection of Collective Bargaining Agreements, supra*, 22 Wayne L. Rev. at 176 (criticizing the *Kevin Steel* standard because it lacked sufficient content to guide the bankruptcy courts in balancing the equities). Thus in its second and definitive examination of the issue the Second Circuit declared that rejection would be permissable "only where it clearly appears to be the lessor of two evils and that, unless the agreement is rejected, the [company] will collapse and the employees will no longer have their jobs." *BRAC* v. *REA Express, supra* at 172. In cases involving petitions to reject labor contracts made under both the superseded Bankruptcy Act and the new Code, the lower courts have faithfully followed the reasoning and ruling of the Second Circuit as expressed in *REA Express*. See, *e.g.*,

Matter of Brada Miller Freight Co., 16 Bnkr. Rptr. 1002, 1014 (N.D. Ala. 1982) (appeal pending in 11th Cir.); *Matter of Allied Technology, Inc.*, 8 Bankr. Rptr. 366, 368 (S.D. Ohio 1980); *Matter of Allied Supermarkets, Inc.*, 6 Bankr. Rptr. 968 (E.D. Mich. 1980); *Bohack Corp.* v. *Local Union No. 807*, 431 F. Supp. 646 (E.D. N.Y.), *aff'd*, 567 F.2d (2d Cir. 1977), *cert. den.*, 439 U.S. 825 (1978); *In re Alan Wood Steel Co.*, 449 F. Supp. 165, 169 (E.D. Pa. 1978), *appeal dismissed*, 595 F.2d 1211 (3d Cir. 1979); *In re Penn Fruit Co.*, 92 L.R.R.M. (BNA) 3548 (E.D. Pa. 1976); *In re Studio Eight Lighting*, 91 L.R.R.M. (BNA) 2429 (E.D. N.Y. 1976); *In re David Rosow, Inc.*, 106 L.R.R.M. (BNA) 2842, 2843 (Bankr. D. Conn. 1981); *In the Matter of the Connecticut Celery Co.*, 106 L.R.R.M. (BNA) 2847 (Bankr. D. Conn. 1981).*

Unmoved by the prospect of this nation's workers innocently losing pension, welfare and seniority rights as a consequence of often incompetent management, and unconvinced by the numerous decisions of the federal courts, the Third Circuit rejected the two-step test formulated in *REA Express*. Describing *REA Express* as the "illegitimate progeny" of *Kevin Steel*, the Third Circuit criticized the Second Circuit for "trampling upon the grave" of *Kevin Steel* (13a, n.11). In place of the allegedly illegitimate *REA Ex-*

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* The tension between the labor and bankruptcy laws was also raised in *Local Joint Executive Board* v. *Hotel Circle, Inc.*, 612 F.2d 210 (9th Cir. 1980). In that case the issues were whether a court even had the authority to reject a labor contract and whether a receiver had the power to enter into a long-term labor contract. The Ninth Circuit ruled that a court did have the authority to reject a labor contract but expressly stated that it was not deciding what the standard for rejection would be. *Local Joint Bd.* v. *Hotel Circle*, 613 F.2d at 213 n.2. In the instant case the petitioner acknowledges that a court does have the authority to approve rejection of a labor contract under §365(a), but only after the provisions of the NLRA were followed. On the issue of the applicable standard of review to be used, the Ninth Circuit's decision is obviously not instructive. In sum, the *Hotel Circle* case is of no heuristic value here.

press standard, the Third Circuit reverted to the lax and vague "weighing of equities" test.

The Third Circuit's perception of the manner in which the equities should be balanced is illuminating, and disheartening. The court explained that, in its view, employees who have given years of service to a company in the expectation that they would be able to retire with a decent income would be willing to completely surrender those benefits simply to keep their jobs (17a). In language redolent of the eighteenth century, the Third Circuit opined that a person would rather work without any fringe benefits than not work at all (17a, n.13). This mean-spirited ideology is not only anachronistic, it is unnecessary.

To be sure, a job without benefits is better than no job at all, but the issue here is whether and when the employee should be compelled to face that harsh choice. The entire point is that the worker should not be confronted with that sad selection unless it is absolutely unavoidable. Indeed, that is the purpose and fairness of the *REA Express* test, and conversely, that is the problem and inequity of the Third Circuit's test. Under *REA Express* a debtor company can obtain rejection of the collective bargaining agreement, but only after it demonstrates that the choice is truly between rejection (and losing all benefits) or losing all jobs. Plainly stated, the *REA Express* stands for this principle: where a debtor company can continue to operate without requiring that workers surrender accrued benefits and work without rights, then fairness and decency preclude a court from approving rejection and depriving those workers of their pension, welfare and seniority rights. Contrary to this, the Third Circuit's formula would allow the utter destruction of essential earned benefits even though it is unnecessary to the debtor company's continued existence.*

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* The foregoing discussion only reinforces the petitioner's argument that rejection of a labor contract under §365(a)

(Footnote continued on following page)

The mere statement of the two standards would seem to compel the choice: should this Court condone the unnecessary derogation of accrued pension, welfare and seniority rights simply to ease the profit picture of a company in bankruptcy or should this Court hold that the destruction of such vital rights may occur only where truly necessary to the continued operation of the company and the existence of jobs. While it may be regrettable that the Second Circuit did not adequately articulate the appropriate standard in its first grapple with this issue, that should not detract from the propriety and soundness of its subsequent rulings. Though repetition does not create validity, the widespread adoption by the lower courts of the *REA Express* standard serves to confirm the correctness of that test. Rather than trampling on *Kevin Steel, REA Express* improved upon it.

Moreover, the uniform adoption and application of the *REA Expres* test by the lower courts undermines the Third Circuit's concern that a bankruptcy court would be unable to predict whether rejection is necessary to avoid the imminent collapse of the company (14a). The bankruptcy and district courts are intimately involved in the bankruptcy process and constantly make assessments regarding the needs and abilities of debtors. The fact that the lower courts throughout the nation have expressly accepted and successfully employed the *REA Express* test lays to rest the fear that that test is unworkable. The lower courts have found the *REA Express* both fair and practical.

(Footnote continued from preceding page)

should not be considered unless the company has first complied with the provisions of the NLRA. As explained above, §8(d) allows the parties the opportunity and right to modify the collective bargaining agreement so as to protect fundamental benefits, such as pensions, while eliminating or reducing other costs. This ability to modify a contract so as to simultaneously protect the workers and permit the company to obtain a more liveable contract is not available under §365(a), which is an all or nothing proposition.

The Third Circuit' refusal to accept the *REA Express* standard has created a direct conflict between the circuits on an issue of tremendous and growing significance throughout the country. It is respectfully but urgently requested that this Court review the Third Circuit's decision and finally resolve this matter.

CONCLUSION

For all of the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari to the United States Court of Appeals for the Third Circuit should be granted.

Respectfully submitted,

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On the Petition.

APPENDIX A

Opinion of the United States Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 81-2140 and 81-2238

In Re: BILDISCO, A General Partnership of the State of New Jersey,

Local 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America
Appellant, No. 81-2140

NATIONAL LABOR RELATIONS BOARD,
Intervenor

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY
(D.C. Civil No. 81-0513)

NATIONAL LABOR RELATIONS BOARD
Petitioner, No. 81-2238

v.

BILDISCO AND BILDISCO,
DEBTOR-IN-POSSESSION,
Respondent

LOCAL 408, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA,
Intervenor

National Labor Relations Board
Application for Enforcement

Argued March 19, 1982

Before: ALDISERT, VAN DUSEN, and GARTH,
Circuit Judges

(Filed June 17, 1982)

Appendix A

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Appendix A

OPINION OF THE COURT

ALDISERT, *Circuit Judge*.

In these consolidated proceedings we are required to accommodate th tension be:ween two important aspects of our national policy, represented by the National Labor Relations Act and the Bankruptcy Reform Act of 1978. Specifically, we must decide whether the bankruptcy court erred in permitting a debtor-in-possession to reject a collective bargaining agreement as an executory contract. We also must consider the National Labor Relations Board's application for enforcement of its order determining that the same debtor-in-possession committed an unfair labor practice by unilaterally changing the terms of the agreement. We vacate the judgment in the appeal at No. 81-2140 and remand for further proceedings. Because the NLRB both erred in its choice and application of legal precepts and abused its discretion, however, we deny the application for enforcement at No. 81-2238.

I.

Bildisco, a New Jersey partnership engaged in selling and distributing building supplies, filed a voluntary petition for reorganization on April 14, 1980, under Chapter 11 of the Bankruptcy Code. The bankruptcy court thereafter designated the partnership as a debtor-in-possession and authorized it to operate the business under 11 U.S.C. §1107.[1]

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1. A debtor-in-possession is the debtor, 11 U.S.C. §1101(1), who is given many additional rights, powers, and duties to the estate, as set forth generally in §1107:

> (a) Subject to any limitations on a trustee under this chapter, and to such limitations or conditions as the court prescribes, a debtor in possession shall have all the rights, other than the right to compensation under section 330 of this title, and powers, and shall perform all the functions and duties, except the duties specified in sections 1106 (a)(2), (3), and (4) of this title, of a trustee serving in a case under this chapter.

Appendix A

Bildisco and Local 408 of the Teamsters Union were parties to a collective bargaining agreement that on the date of the petition covered eighteen of Bildisco's employees. On January 5, 1981, the debtor-in-possession sought bankruptcy court permission to reject the collective bargaining agreement under 11 U.S.C. §365(a), which permits rejection of executory contracts upon bankruptcy court approval. The sole witness at the hearing on the motion was one of Bildisco's partners, Sal Valente, who testified that Bildisco's creditors were concerned about the "union situation" and that by operating without the collective bargaining agreement Bildisco would be able to save approximately $100,000 in 1981. Although eighteen of Bildisco's employees were covered by the collective bargaining agreement as of the date of the petition, by the date of the hearing the number had been reduced to three.[2] The union cross-examined Valente, but it did not offer any other evidence concerning the effect of rejection on Bildisco's employees.

The bankruptcy judge, without expressly articulating the standard that he applied,[3] granted permission to

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2. Valente estimated that Bildisco would be increasing the number of employees to ten as the off-season ended, and his projections of the savings that would be realized if the agreement were rejected are predicated on the costs of salaries and benefits to ten employees.

3. The bankruptcy judge concluded his consideration of the standard to be applied as follows:

> I don't know under the Code what power the court has to disapprove an application to reject a contract, unless it can be shown it was a promiscuous act on the part of the debtor, and it was really a beneficial contract.
>
> It is surely not a beneficial contract if it costs him $132 a week, which is my own computation, more than he would have to pay if he didn't have the contract.
>
> Under the circumstances I am going to have to allow the motion of the debtor.

reject on January 15, 1981, retroactive to the date immediately preceding the date of the petition. *See* 11 U.S.C. §365(g)(1). The union appealed to the district court, which on May 4, 1981, issued a bench opinion affirming the order of the bankruptcy court. Noting that the bankruptcy judge had not identified the test he had used, the district court held that the permission to reject was proper in any event.

In the meantime, the union had filed unfair labor practices charges with the NLRB complaining that Bildisco had refused to grant certain wage increases, to pay pension and welfare contributions, or to turn over union dues, all in violation of the collective bargaining agreement. After investigating the charges, the General Counsel of the NLRB issued a complaint on July 31, 1980, alleging that Bildisco, and Bildisco as debtor-in-possession, had engaged in unfair labor practices in violation of sections 8(a)(1) and (5) of the National Labor Relations Act by making unilateral changes in the collective bargaining agreement. The complaint advised Bildisco that a hearing had been scheduled for March 9, 1981, more than seven months later, and that if Bildisco did not answer the complaint within ten days of service, all of the allegations would be deemed admitted. On September 24, 1980, a Board agent advised Valente of the company's obligation to answer the com-

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App. at 62-63. Subsequently, the following dialogue took place:

> COUNSEL FOR THE UNION: Just for the record, your Honor, with respect to the ruling today, it is your position, your Honor — and correct me if I am wrong — the cases prior to the enactment of the Bankruptcy Code, those cases dealing with special considerations given collective bargaining are no longer applicable?
>
> . . . .
>
> THE COURT: All I am saying is this is not a case under the Bankruptcy Act; it is under the Bankruptcy Code.
>
> Under Section 365 I have to grant the motion to reject.

App. at 64-65.

plaint. On October 8, the General Counsel issued an amended complaint reflecting additional union allegations that the company had failed to pay vacation benefits to its employees. On October 27, 1980, a Board attorney informed Valente by telephone and by letter that he would seek summary judgment if no answer to the amended complaint were received by October 31. No answer was filed.

On January 27, 1981, twelve days after the bankruptcy court authorized rejection of the collective bargaining agreement, the Board's General Counsel moved for summary judgment based on Bildisco's failure to answer the amended complaint. Two days later Bildisco responded with a request for a 60-day stay of proceedings so that it could apply for bankruptcy court permission to retain special labor counsel. The General Counsel opposed this request.

On February 9, 1981, the Board issued a notice to show cause why summary judgment should not be granted. Bildisco responded on February 20 that its delay in filing an answer was caused by the disruption of Chapter 11 proceedings and that it had not yet received bankruptcy court permission to retain special labor counsel.[4] It also informed the Board that the bankruptcy court had granted its motion for permission to reject the collective bargaining agreement. Noting the retroactive effect of the rejection, the debtor-in-possession argued that no contract existed between it and the union after April 14, 1980. It argued also that any unpaid contributions due prior to the petition did not constitute unilateral changes in the contract, but were claims subject to allowance in Bildisco's Chapter 11 proceeding.

On April 23, 1981, stating that Bildisco had not shown good cause for failing to file a timely answer, the Board granted the General Counsel's motion for sum-

4. The bankruptcy court granted Bildisco this permission on April 16, 1981.

mary judgment, notwithstanding its notification two months earlier that the bankruptcy court had permitted Bildisco to reject the agreement. The order, addressed to "Bildisco and Bildisco, debtor-in-possession," required Bildisco to make all the delinquent contributions and payments plus interest, to honor the terms of the collective bargaining agreement, and to post appropriate notices. The NLRB made a "finding of fact" that the debtor-in-possession "is, and has been at all times material herein since April 17, 1980, an alter ego in bankruptcy to Bildisco." App. at 131.[5] The Board subsequently applied to this court for enforcement of its order.

We granted the Board's motion to consolidate the two cases. The Board has intervened in the union's appeal from the district court order, and the union has intervened in the Board's application for enforcement. We will consider the appeal and the application for enforcement in turn.

II.

The rejection of a collective bargaining agreement under the new Bankruptcy Code, which implicates a significant confrontation of labor and bankruptcy policies, is a matter of first impression in the courts of appeals. Nevertheless, we have the benefit of both statutory direction and the decisions of other courts interpreting the equivalent section of the former Bankruptcy Act and the relevant provisions of the NLRA.

A.

Underlying Chapter 11 of the Code is a legislative policy to provide opportunities for a debtor to reduce or extend debts so that it can return to financial viability.

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5. The respondent filed a motion for reconsideration accompanied by an answer to the Board's complaint; the Board rejected the motion because it was postmarked two days after the deadline for such motions. *See* 29 C.F.R. §102.48(d)(2).

> The purpose of a business reorganization case, unlike a liquidation case, is to restructure a business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders. The premise of a business reorganization is that assets that are used for production in the industry for which they were designed are more valuable than those same assets sold for scrap. Often, the return on assets that a business can produce is inadequate to compensate those who have invested in the business. Cash flow problems may develop, and require creditors of the business, both trade creditors and long-term lenders, to wait for payment of their claims. If the business can extend or reduce its debts, it often can be returned to a viable state. It is more economically efficient to reorganize than to liquidate, because it preserves jobs and assets.

H.R. Rep. No. 595, 95th Cong., 1st Sess. 220 (1977), *reprinted in* 1978 U.S. Code Cong. & Ad. News 5963, 6179. If a business can be turned around by reorganization, its creditors will recover more on their claims than in a Chapter 7 liquidation,[6] its employees will keep their jobs, and the public will continue to benefit from its production. Thus the debtor, its creditors and employees, and the public at large benefit from the business' surviv-

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6. Experience under the Bankruptcy Act demonstrated that creditors received larger portions of their claims from reorganization proceedings than from liquidations. According to tabulations taken from a sample of bankruptcy cases, priority creditors usually received full payment in a successful reorganization but realized less than one-third of the amount of their claims in a straight bankruptcy. Unsecured creditors realized only a median nineteen percent under one-payment plans and ten percent under deferred payment plans when the debtor went through reorganization, but in straight bankruptcies the median was only eight percent. D. Stanley & M. Girth, Bankruptcy: Problem, Process, Reform 129-30, 142-43 (1971).

al. Under the congressional schema, this goal is promoted by numerous specific mechanisms, including continued operation in the hands of the debtor-in-possession or trustee, under supervision of the court, with a "breathing spell" free from the collections efforts of creditors. Another mechanism is to allow the debtor-in-possession to reject executory contracts that would burden the estate. *See* 2 Collier on Bankruptcy ¶¶365.01.-03 (15th ed. 1981). *See generally Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R.R. Co.*, 318 U.S. 523, 549-51 (1943); *Sparhawk v. Yerkes*, 142 U.S. 1, 13 (1891); *In re Italian Cook Oil Corp.*, 190 F.2d 994 (3d Cir. 1951).

Section 365(a) of the Code provides, with exceptions not now relevant, that "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."[7] Under Chapter 11 a debtor-in-possession has essentially the same powers as a trustee,[8] and it therefore may reject executory contracts with the authorization of the bankruptcy court.

B.

This case places the statutory policies underlying Chapter 11 in tension with our national labor policy, as expressed in the National Labor Relations Act. Broadly

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7. The analogous provision of the Bankruptcy Act stated:

> Upon the filing of a petition, the court may, in addition to the jurisdiction, powers, and duties conferred and imposed upon it by this chapter—
>
> (1) permit the rejection of executory contracts of the debtor, upon notice to the parties to such contracts and to such other parties in interests as the court may designate. . . .

Bankruptcy Act of 1898, §313, 11 U.S.C. §713 (1976) (repealed).

8. 11 U.S.C. §1107. Under certain circumstances the court may appoint a trustee to operate the business. 11 U.S.C. §§1104, 1108.

stated, that policy is to promote industrial peace by facilitating collective bargaining. Sections 7 and 8 of the NLRA, 29 U.S.C. §§157 and 158, guarantee the rights of workers to organize and to bargain collectively and protect both employees and employers from unfair labor practices that undermine these rights.

The specific statute relied on by the union and the Labor Board is §8(d) of the NLRA, which provides that no party to a collective bargaining agreement may "terminate or modify" the agreement without following a specified procedure.[9] Our task is to reconcile the apparent conflict between the NLRA and the Bankruptcy Code and the policies they represent.

III.

In enacting §365, Congress provided no indication that collective bargaining agreements were to be immune from rejection and thus unique among executory

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9. Termination or modification of a collective bargaining agreement is permitted by §8(d) only if the moving party

> (1) serves a written notice upon the other party to the contract . . .;
>
> (2) offers to meet and confer with the other party for the purpose of negotiating a new contract or a contract containing the proposed modifications;
>
> (3) notifies the Federal Mediation and Conciliation Service . . . and . . . any State or Territorial agency established to mediate and conciliate disputes within the State or Territory . . .;
>
> (4) continues in full force and effect, without resorting to strike or lock-out, all the terms and conditions of the existing contract for a period of sixty days after such notice is given or until the expiration date of such contract, whichever occurs later: . . . [T]he duties so imposed shall not be construed as reqll not be construed as requiring either party to discuss or agree to any modification of the terms and conditions contained in a contract for a fixed period, if such modification is to become effective before such terms and conditions can be reopened under the provisions of the contract.

29 U.S.C. §158(d).

contracts. Indeed, the few inferences of congressional intent that may be gleaned from the Code and its legislative history are to the contrary. First, notwithstanding several judicial decisions holding collective bargaining agreements susceptible to rejection.[10] Congress afforded collective bargaining agreements no special treatment. Significantly, Congress did provide detailed provisions for acceptance of executory contracts such as shopping center leases, §365(b)(3), and regarding transactions in commodities futures contracts, §§765, 766. Moreover, one particular species of collective bargaining agreement was singled out:

> Notwithstanding section 365 of this title, neither the court nor the trustee may change the wages or working conditions of employees of the debtor established by a collective bargaining agreement that is subject to the Railway Labor Act (45 U.S.C. 151 et seq.) except in accordance with section 6 of such Act (45 U.S.C. 156).

11 U.S.C. §1167. The sheer complexity of the Bankruptcy Reform Act might preclude our use of §1167 as definitive proof that every other collective bargaining agreement may be rejected, but the section permits an inference that, with this one exception, Congress did not intend to distinguish collective bargaining agreements from executory contracts in general.

IV.

Having determined that §365(a) authorizes the bankruptcy court to permit the rejection of collective

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10. *See, e.g., Truck Drivers Local Union No. 807 v. Bohack Corp.*, 541 F.2d 312 (2d Cir. 1976); *Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc.*, 523 F.2d 164 (2d Cir.), *cert. denied*, 423 U.S. 1017, 1073 (1975); *Shopmen's Local Union No. 455 v. Kevin Steel Products, Inc.*, 519 F.2d 698 (2d Cir. 1975); *Local Joint Executive Board, AFL-CIO v. Hotel Circle, Inc.*, 419 F.Supp. 778 (S.D. Cal. 1976), *aff'd*, 613 F.2d 210 (9th Cir. 1980).

bargaining agreements, we now turn to the standards it should use in considering such a request. We begin by rejecting the concept that the proceeding under §8(d) of the NLRA is mandated. As more fully developed in Part VI-A, *infra*, a debtor-in-possession is a new entity, separate and apart from the pre-bankruptcy company, and does not become a party to an executory contract unless it assumes the contract. Bildisco, as a debtor-in-possession, was not a party to the collective bargaining agreement, and therefore not bound by §8(d). *Shopmen's Local Union No. 455 v. Kevin Steel Products, Inc.*, 519 F.2d 698, 704 (2d Cir. 1975). The burden of persuading the bankruptcy court to permit rejection of a collective bargaining agreement must be placed on the moving party: the debtor-in-possession or the trustee. Our critical task is to establish the extent of that burden.

A.

The usual test for rejection of an executory contract is simply whether rejection would benefit the estate, the "business judgment" test. *See* 2 Collier on Bankruptcy ¶365.03 (15th ed. 1981). The impact of rejection of a collective bargaining agreement on the rights of workers and the favored status those rights have been accorded by Congress, however, require a more stringent examination of the evidence offered to justify rejection of such a contract. The second circuit in *Kevin Steel*, speaking through Judge Feinberg, accommodated the interests of the workers by holding that rejection of a collective bargaining agreement requires " 'thorough scrutiny, and a careful balancing of the equities on both sides.' " 519 F.2d at 707 (quoting *In re Overseas National Airways, Inc.*, 238 F.Supp. 359, 361 (E.D.N.Y. 1965)).

We accept this formulation of the appropriate relationship between the competing statutory policies. It accommodates the statutory polices of the Labor Act by demanding a greater evidentiary showing than for

rejection of a typical executory contract, but it does not erect impossible barriers to rejection of labor contracts in violation of the policies underlying Chapter 11. It plots a middle course between the possible extremes, requiring a sensitive weighing of the competing private and public interests in the context of the particular case.

We reject, however, the formulations of subsequent decisions pressed on us by the union and the Board, which purport to follow the rule of *Kevin Steel* but instead replace its "balancing of the equities" with a test predicating permission to reject on a showing "that an onerous and burdensome executory collective bargaining agreement will thwart efforts to save a failing carrier in bankruptcy from collapse." *Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc.*, 523 F.2d 164, 169 (2d Cir.), *cert. denied*, 423 U.S. 1017, 1073 (1975).[11] According to *REA Express*, rejection should be permitted "only where it clearly appears to be the lesser of two evils and that, unless the agreement is rejected, the carrier will collapse and the employees will no longer have their jobs." *Id.* at 172. The district court in this case and the court in *In re Alan Wood Steel Co.*, 449 F.Supp. 165 (E.D.Pa. 1978), *appeal dismissed*, 595 F.2d 1211, 1214 (3d Cir. 1979), apparently building on *REA Express* and *In re Penn Fruit Co.*, 92 L.R.R.M.

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11. They reflect a phenomenon that our distinguished, former colleague, the late William H. Hastie, called "trampling upon graves": adding a substantial gloss to a previously stated holding but improperly citing the former case as the authority for the new formulation. Of course, the development of the law often consists of adding gloss to previous cases, as Cardozo described it: "Given a mass of particulars, a congeries of judgments on related topics, the principle that unifies and rationalizes them has a tendency, and a legitimate one, to project and extend itself to new cases within the limits of its capacity to unify and rationalize." B. Cardozo, The Nature of the Judicial Process 31 (1921). But it is quite another thing to disguise an expansion of the law by pretending that the court is simply applying a previously stated rule of law.

(BNA) 3548 (E.D. Pa. 1976), declared that *Kevin Steel* required a two step analysis:

> First, the court should determine that the agreement is onerous and burdensome to the estate, *so that failure to reject will make a successful arrangement impossible*. Second, the equities must be balanced and found to favor the debtor. Then, and only then, may rejection of a collective bargaining agreement be permitted.

449 F. Supp. at 169, *quoted in* district court op. at 4-5 (emphasis added).

The italicized portion of the first step, in our view, goes well beyond the "balancing of equities" required by *Kevin Steel*. We reject this more stringent test for two discrete but related reasons: first, for the pragmatic reason that it may be impossible to predict the success *vel non* of a reorganization until very late in the arrangement proceedings; and second, for the prudential consideration that the imposition of such a test unduly exalts the perpetuation of the collective bargaining agreement over the more pragmatic consideration of whether the employees will continue to have jobs at all.

At the date of oral argument in these proceedings, March 19, 1982, Bildisco was still operated by a debtor-in-possession under the supervision of the bankruptcy court. Thus almost two years after the petition for reorganization was filed and over a year after the court granted the debtor-in-possession permission to reject the agreement, there is still no assurance that Bildisco will successfully reorganize. We simply do not and cannot know whether it will be forced into liquidation. It is entirely unrealistic to require the bankruptcy court at an early stage of a reorganization proceeding to predict whether reorganization will be impossible absent rejection of the labor contract. In the common law tradition the acceptability or durability of a legal rule is directly dependent upon its utility. The rule urged upon us by

the NLRB and the union appears to us deficient because we know of no formula readily available to a bankruptcy court in an early stage of a Chapter 11 reorganization that could reasonably predict whether a business reorganization will succeed.

We also reject the more stringent test because it could work to the detriment of the workers it seeks to protect. By erecting an excessive evidentiary barrier to rejection of labor contracts, the *REA Express-Alan Wood Steel* formulation would make it likely that numerous businesses attempting to reorganize will in fact be forced over the line into liquidation. Adherence to a collective bargaining agreement together with a successful reorganization is surely the best of possible worlds; but given the inevitable potential for conflict between these goals we think it preferable that jobs be preserved through rejection of a labor contract than that they be lost because of its acceptance.

In the multiplicity of fact situations that will arise, we think our best option is to require the bankruptcy courts to undertake a "thorough scrutiny, and a careful balancing of the equities on both sides" as set forth in *Kevin Steel*. Each case will present its own complexities. For example, the bankruptcy court must understand that the debtor-in-possession who rejects a collective bargaining agreement remains an employer and is still required by the NLRA to bargain with the representatives of its employees, *Kevin Steel*, 519 F.2d at 704, and that its employees retain their right to strike should negotiations fail, *see In re Ryan Co.*, 83 Lab.Cas. (CCH) ¶10,487 at 17,952 n.2 (D.Conn. 1978). The consequences of a strike on a precarious business therefore must be one factor to be weighed by the bankruptcy court. Moreover, because under §365(g) rejection constitutes a breach of contract, the employees may assert a claim for the value of the benefits lost. The court should consider both the impact of the resulting claim against

the debtor and the adequacy of the relief employees might obtain through the claims procedures.[12]

B.

We are satisfied that *Kevin Steel*, isolated from its illegitimate progeny, provides the appropriate framework for an intelligent and equitable approach to the problem because it gives collective bargaining agreements a measure of protection beyond that available under the business judgment test without unduly advancing the interests served by the Labor Act over the other interests of the employees and those of the debtor's other creditors. We believe that the debtor-in-possession must first demonstrate that the continuation of the collective bargaining agreement would be burdensome to the estate; that once this threshold determination has been made the debtor-in-possession must make a factual presentation sufficient to permit the bankruptcy court to weigh the competing equities; that the polestar is to do equity between claims which arise under the labor contract and other claims against the debtor; that, in this, the court must consider the rights of covered employees as supported by the national labor policy as well as the possible "sacrifices which other creditors are making" in the effort to bring about a successful reorganization, *Group of Institutional Investors*, 318 U.S. at 550; and that the court must make a reasoned determination that rejection of the labor contract will assist the debtor-in-possession or

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12. Among other factors bankruptcy courts might consider in balancing the equities are, for example, the proportion of the debtor's employees covered by the collective bargaining agreement, how those employees' wages and benefits compare to those of others in the industry, and the good or bad faith of the parties in dealing with the effect of the company's insolvency on its labor obligations. *See* Note, *The Bankruptcy Law's Effect on Collective Bargaining Agreements*, 81 Colum. L. Rev. 391, 401-03 (1981). The listing of these considerations is not intended to be all-inclusive.

the trustee to achieve a satisfactory reorganization. We believe that particularly in a time of economic uncertainty and distress an analysis following this pattern provides more protection to both employer and employee than the test urged upon us by the union and the NLRB.[13]

V.

Having identified the considerations properly applicable to rejections of collective bargaining agreements, we turn to the appeal at No. 81-2140; and we begin by examining the arguments presented to the bankruptcy court. The union argued that the proper test was that articulated in *REA Express* and *Alan Wood Steel:* rejection is permissible only if reorganization otherwise would be impossible and if the equities favor the debtor. Counsel for the debtor-in-possession, on the other hand, submitted that collective bargaining agreements are to be treated like all other executory contracts and that rejection

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13. According to data supplied by the U.S. Department of Labor, as of February, 1982, 9.6 million Americans wanting to work were unable to find jobs. This constitutes 8.8% of the work force and an increase from 3.4% in January-March 1969, 4.6% in October 1973, and 5.7% in May-July 1979. Because Bildisco is involved in the building supply business, a business directly associated with the construction business, and the employees who are covered by the labor contract are warehousemen, drivers, mechanics, and outside field servicemen, it is significant that 18.1% of the nation's construction workers were unemployed compared with 12.5% of blue-collar workers in general. U.S. News & World Report, March 15, 1982, at 71-73. Under circumstances of a distressed economy, a bankruptcy court could properly consider that it would be in the interests of the workers in a bargaining unit to be afforded the opportunity to continue to work under less generous financial benefits than to insist upon an absolute payment of vacation benefits, pension, health and welfare benefits, and wage increases. In weighing the equities the court could well conclude that it is in the public interest for employees to work without the advantage of fringe benefits than not to work at all.

should be permitted whenever it would benefit the debtor.

The bankruptcy court's bench opinion unfortunately was a woefully inadequate treatment of a sophisticated subject. It is not clear whether the bankruptcy court chose one of the two standards proffered by the parties or applied a synthesis of the two.[14] Where the state of the law is settled there are three critical prerequisites to a determination of reversible error: (a) specific acts or omissions by the trial court constituting legal error, (b) properly suggested as error to the trial court, and (c), if uncorrected on that level, then properly presented for review to the appellate court. Assuming that the trial court erred, for there to be reversible error, we must be able to determine that appellant properly identified the error and requested the trial court to take a legally appropriate course of action. *Pfeifer v. Jones & Laughlin Steel*, ____ F.2d ____, ____ n.1, No. 81-1928 (3d Cir. April 16, 1982), slip op. at 6 n.1. In the district courts, Fed.R.Civ.P. 46 requires a party to "[make] known to the court the action which he desires the court to take or his objection to the action of the court and his grounds therefor." This requirement affords an opportunity for error correction and avoidance in the trial court in various ways: It gives the adversary the opportunity either to avoid the challenged action or to present a reasoned defense of the trial court's action, and it provides the trial court with the alternatives of modifying its decision or of ordering a more fully developed record for review. It also challenges the court to articulate the grounds for its decision and thus facilitates appellate review.

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14. The district court affirmed the bankruptcy court by determining that, applying either test, the contract was appropriately rejected. The district court's analysis need not detain us, however, because our role as a court of review is identical to that of the district court. *Universal Minerals, Inc. v. C. A. Hughes & Co.*, 669 F.2d 98, 101-02 (3d Cir. 1981).

Where the state of the law is not settled, and the court of the first instance has not set forth a reasoned elaboration for its decision, as here, an appellate court cannot determine what motivated the trial court's decision. It cannot properly determine whether there was a specific act or omission constituting legal error. Even though an appellate court can affirm on the basis of reasons different from those set forth by the trial court, *Rhoads v. Ford Motor Co.*, 514 F.2d 931 (3d Cir. 1975), a reviewing court cannot properly perform its function until the parties are given the opportunity to prepare a record and the trial court the opportunity to apply in the first instance newly formulated precepts to the facts adduced. Because we have set forth in detail the appropriate precepts to apply in a hitherto unsettled area of the law, and because we do not have the benefit of an adequate explanation of the trial court's action, the preferable course is to remand the proceedings for reconsideration in light of the precepts we announce today. Accordingly, we vacate the judgment of the district court and remand to it with a direction that the cause be further remanded to the bankruptcy judge for reconsideration.

VI.

We now turn to the Board's application at No. 81-2238 for the enforcement of its summary judgment determining that the debtor-in-possession had committed an unfair labor practice.

It must be emphasized that we are not faced with an application for enforcement of an NLRB order entered after reception of evidence by an administrative law judge and a review of the record by the Board. We have only an application for enforcement of summary judgment; our denial of enforcement does not preclude the Board from processing the charges through a full hearing, guided and governed by the bankruptcy court's de-

termination on remand concerning the rejection of the collective bargaining agreement, and by the views which we have expressed in this opinion.

A.

The basis of the unfair labor practice charges is an allegation that the debtor-in-possession unilaterally changed the terms of the collective bargaining agreement and thereby failed to bargain in good faith, in violation of sections 8(a)(1) and (5) of the NLRA. The Board's theory depends upon its contention that the debtor-in-possession is an alter ego of the debtor and thereby a party to the collective bargaining agreement. The Board's argument fails, however, because, as a matter of law, a debtor-in-possession is "[a] new entity . . . created with its own rights and duties, subject to the supervision of the bankruptcy court." *Kevin Steel*, 519 F.2d at 704 (footnote omitted). A debtor-in-possession is given powers comparable to those of a trustee, and it is thus an officer of the court. 11 U.S.C. §1107. As the House and Senate Reports explaining §1107 emphasize:

> This section places a debtor in possession in the shoes of a trustee in every way. The debtor is given the rights and powers of a chapter 11 trustee. He is required to perform the functions and duties of a chapter 11 trustee (except the investigative duties). He is also subject to any limitations on a chapter 11 trustee, and to such other limitations and conditions as the court prescribes.

H. R. Rep. No. 595, 95th Cong., 1st Sess. 404 (1977), *reprinted in* 1978 U.S. Code Cong. & Ad. News 5963, 6360; S. Rep. No. 989, 95th Cong., 1st Sess. 116 (1978), *reprinted in* 1978 U.S. Code Cong. & Ad. News 5787, 5902. The debtor-in-possession's position is analogous to that of a successor employer: it may be required to recognize and bargain with the union, but it is not a party to

its predecessor's collective bargaining agreement unless it assumes that agreement. *NRLB v. Burns Security Services, Inc.*, 406 U.S. 272, 284 (1972); *Kevin Steel*, 519 F.2d at 704. Because Bildisco as debtor-in-possession is not a party to the agreement with Local 408, it had the ability to reject the agreement without following the procedures outlined in §8(d). We suggest to the NLRB that, at least in matters within this judicial circuit, it cease operating under such a fundamental misconception of the law. Indeed, we believe that persisting in such a misconception — one that goes to the difference between the pre-bankruptcy company which was the signatory to the collective bargaining agreement and the succeeding debtor-in-possession — is so fundamental that this error in and of itself is sufficient reason to refuse to enforce a summary judgment so predicated.

B.

The Board contends, however, that this court may not consider Bildisco's defenses to the unfair labor practice complaint because they were not urged before the Board in a timely manner. Section 10(e) of the NLRA, 29 U.S.C. §160(e), provides that "[n]o objection that has not been urged before the Board, its member, agent or agency, shall be considered by the court, unless the failure or neglect to urge such objection shall be excused because of extraordinary circumstances"; and the Supreme Court has consistently held that, in the absence of extraordinary circumstances, "the failure or neglect of a respondent to urge an objection in the Board's proceedings forecloses judicial consideration of the objection in enforcement proceedings." *NLRB v. Ochoa Fertilizer Corp.*, 368 U.S. 318, 322 (1961). The Board contends that the debtor-in-possession's sole excuse for its failure to file an answer was the disruption in its operations caused by reorganization proceedings, and that this excuse would not come within §10(e)'s "extraordinary circumstances" exception.

We hold that § 10(e) is inapplicable to this case because the objection was urged before the Board at a time when the Board could have taken meaningful notice of it. Inasmuch as the date of the hearing had not yet passed, the Board's draconian remedy was unwarranted. We have recently observed that

> an administrative agency like the NLRB, burdened with an extremely heavy caseload, must necessarily rely upon compliance with procedural rules to function efficiently. As part of the process, reasonable time limitations must be set and observed. Nevertheless, there are instances where wooden and unreasoning insistence upon technical procedural rules results, not in the proper disposition of a cause, but in injustice. Failure to take remedial measures when such incidents occur constitutes an abuse of discretion.

Livingston Powdered Metal, Inc. v. NLRB, 669 F.2d 133, 137 (3d Cir. 1982). We recognize that the response to the complaint here was exceedingly tardy, more so than in *Livingston* or its companion case of *Kessler Institute for Rehabilitation v. NLRB*, 669 F.2d 138 (3d Cir. 1982). But in *National Book Consolidators, Inc. v. NLRB*, 672 F.2d 323 (3d Cir. 1982), we required the Board to "utilize a 'good cause' standard in determining whether to accept filing of an answer," explaining that " '[t]he purpose of the "good cause" standard . . . is to ensure that the Board makes decisions on the merits despite technical and inadvertent noncompliance with procedural rules.' " *Id.* at 326 (quoting *NLRB v. Zeno Table Co.*, 610 F.2d 567, 569 (9th Cir. 1979)).

We do not suggest that the mere fact that a debtor-in-possession is implicated in the proceedings is itself sufficient reason for a delay. But the drastic circumstances here, where a work force of eighteen union members had been reduced to three in a business intimately associated with the construction industry, one of

the most distressed industries of the present recession, and where the pre-bankruptcy company had been in active reorganization by a debtor-in-possession for over a year, we believe that the Board was presented with a "good cause" for accepting an untimely response and proceeding to consider what appears to us to be a most persuasive argument on the merits.

The timetable is significant. The amended complaint was filed October 8, 1980, and set a March 9, 1981, hearing date. On February 20, 1981, responding to the Board's order to show cause, Bildisco notified the Board that the bankruptcy court had entered an order on January 15, 1981, granting its motion to reject the labor contract. We do not condone the failure of the debtor-in-possession to respond to the complaint, but we will not enforce a Board order that cavalierly refuses to recognize an outstanding federal court order directly relating to the proceedings before it. Because rejection related back to the day before the Chapter 11 petition was filed, 11 U.S.C. §365(g)(1), no labor contract effectively existed between the union and the debtor-in-possession, subsequent to April 14, 1980. In its thirteen page decision and order dated April 23, 1981, however, the Board failed even to acknowledge, much less to consider the effect of, the bankruptcy court order permitting rejection.

The Board did not explain how, as an agency of the executive branch, it can ignore the order of a federal court. We perceive no excuse for this disregard. It is as much a departure from acceptable decision-making for the NLRB to decide a case within its competence without accommodating competing principles of bankruptcy law as it would be for a bankruptcy court to decide a labor contract issue without accommodating competing principles of our national labor policy. Whatever the debtor-in-possession's technical breach of the NLRB's procedural rules, it does not excuse the agency's refusal to recognize the existence of the outstanding bankrupt-

cy court order and to give some explanation why that order would be irrelevant to its proceedings.

We therefore conclude, for all the foregoing reasons, that the NLRB both erred as a matter of law and misused its discretion in granting the motion for summary judgment. Because the summary judgment included pre-petition charges as well as those relating to activities subsequent to the filing of the bankruptcy petition, it will be for the NLRB in the first instance to separate the two types of charges at any subsequent proceeding. Where charges of unfair labor practices arise both before and after the date of a Chapter 11 petition, the rejection of a collective bargaining agreement would not affect the obligations of the employer under §8(d) prior to the date of the petition. We agree with the Board that a monetary claim resulting from a Board order in such circumstances is governed by bankruptcy law and may be filed as the claim of a creditor in the bankruptcy court. *See* Reply Br. at 7.

It would seem, however, that the Board must await the determination of the bankruptcy court on remand before it may proceed to consider the post-petition charges. If under the precepts we announce today the bankruptcy judge again permits the rejection of the collective bargaining agreement, the Board will be bound by that determination, which would preclude any post-petition unfair labor practice arising from the rejected agreement.

VII.

The judgment of the district court at No. 81-2140 will be vacated and the cause remanded to it with a direction of a further remand to the bankruptcy judge for reconsideration in light of the foregoing. The NLRB's

application for enforcement at No. 81-2238 will be denied without prejudice, for the reasons hereinabove expressed.

A True Copy:

Teste:

Clerk of the United States Court of Appeals
for the Third Circuit

APPENDIX B

Judgment of the United States Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

Nos. 81-2140 and 81-2238

In Re: BILDISCO, A General Partnership of the State of New Jersey,

Local 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America

Appellant, No. 812140

NATIONAL LABOR RELATIONS BOARD,

Intervenor

Appeal from the United States District Court for the District of New Jersey

(D.C. Civil No. 81-0513)

NATIONAL LABOR RELATIONS BOARD,

Petitioner, No. 81-2238

vs.

POSSESSION,
BILDISCO AND BILDISCO, DEBTOR-IN-

Respondent

Appendix B

LOCAL 408, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMAN AND HELPERS OF AMERICA,

Intervenor

National Labor Relations Board
Application for Enforcement

Present: ALDISERT, VAN DUSEN and GARTH, Circuit Judges.

JUDGMENT

These causes came on to be heard on the records from the United States District Court for the District of New Jersey and from the National Labor Relations Board and were argued by counsel on March 19, 1982.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court entered May 6, 1981, be, and the same is hereby vacated and the cause remanded to the said District Court for further remand to the Bankruptcy Court for reconsideration in light of the opinion of this Court.

It is further ordered and adjudged that the National Labor Relations Board's application for enforcement, filed August 6, 1981, be, and the same is hereby denied.

Costs taxed against petitioner in C.A. No. 81-2238.

Attest:

Sally Mrvos
Clerk

June 17, 1982

APPENDIX C

Opinion of the United States District Court for the District of New Jersey

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF NEW JERSEY

Civil Action No. 81-513

In Re:

BILDISCO, A General Partnership of the State of New Jersey,

May 4, 1981
Trenton, New Jersey

BEFORE:

The Honorable Anne E. Thompson, U.S.D.J.

APPEARANCES:

Zazzali, Zazzali & Kroll, Esqs.
By: Albert G. Kroll, Esq.
For Local 408

Ravin, Katchen & Greenberg, Esqs.
By: Jack M. Zackin, Esq.
For the Debtor

The Court: This is an appeal from an Order of the United States Bankruptcy Court for the District of New

Jersey filed on January 15, 1981. In that order, the Bankruptcy Court granted the motion of Bildisco, Debtor in Possession, to reject a May 1, 1979 collective bargaining agreement between Bildisco and Local 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America ("Union"). An appeal to this Court from that order followed.

The standard under which we must review a ruling by the Bankruptcy Court is set out in Rule 810 of the Rules of Bankruptcy Procedure:

> Upon an appeal the district judge may affirm, modify or reverse a referee's judgment or order, or remand with instructions for further proceedings. The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge the credibility of the witnesses.

"If there is a reasonable basis in the record for a bankruptcy judge's ultimate findings of fact, a reviewing court cannot substitute its own ultimate findings of fact simply because it regards its views as effecting a more desirable result than that reached by the bankruptcy judge." *In re Botany Industries,* 463 F. Supp. 793, 795 (ED Pa 1978); *In re Hollock,* 1 B.R. 212, (M.D. Pa. 1979). As a practical matter, what this means is that a

> finding is "clearly erroneous" when although there is evidence to support it, the reviewing court is left with the definite and firm conviction that a mistake has be committed.

United States v. *United Gypsum Co.,* 333 U.S. 364, 395 (1948); *In re Knight,* 421 F. Supp. 1387, 1390 (M.D.La.) (1976).

Appendix C

Under Section 365 of the Bankruptcy Code, 11 U.S.C. §365, a trustee or a debtor in possession is given the right to reject executory contracts in this language:

> Except as provided (elsewhere), the trustee subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

The case of *Shopmen's Union No. 455* v. *Kevin Steel Products*, 519 F. 2d 698 (2d Cir. 1975) was the leading opinion dealing with the rejection of collective bargaining agreements under the old Bankruptcy Act. Under the New Bankruptcy Code, it is not settled whether the standards developed in *Kevin Steel* and those cases which followed it are still applicable to the rejection of executory contracts. Because we find that the lower court's order meets both the old and the proposed new standards, we do not find it necessary to resolve this question.

If Section 365 does not incorporate the *Kevin Steel* standard, then it is likely that collective bargaining agreements will not be treated any differently under §365 than any other executory contracts. This being so, the so-called "business judgment test" for their rejection would apply. Under this test, "(i)t is enough, if, as a matter of business judgment, rejection of the burdenome contract may benefit the estate." *Matter of Minges*, 602 F. 2d 38, 43 (2d Cir. 1979).

Under the record as it stands we find ample justification for the Bankruptcy Court to make the finding that a rejection by the debtor of the collective bargaining agreement would be a sound exercise of its business judgment. Rejection would result in a savings of approximately $100,000. (T. 7) This alone would appear to justify rejection under the "business judgment" test.

On the other hand, it may be that Congress intended to preserve the special treatment accorded to collective bargaining agreements under former Section 313, (now 365). As set forth in *Kevin Steel* and its progeny,

> The cases suggest that a two step analysis be employed by the bankruptcy court in deciding whether to permit rejection of a collective bargaining agreement . . . (citations omitted) . . . First, the court should determine that the agreement is onerous and burdensome to the estate, so that failure to reject will make a successful arrangement impossible. Second, the equities must be balanced and found to favor the debtor.

Matter of Alan Wood Steel Co., 449 F. Supp. 165, 169 (E.D. Pa. 1978).

The Bankruptcy Court did not make a specific finding as to the test to be applied in the rejection of the collective bargaining agreement. It merely notes that "this is not a case under the Bankruptcy Act; it is under the Bankruptcy Code." (Tr. 36). However, we feel that there was evidence before the Bankruptcy Court upon which it could reasonably base the findings required by the *Kevin Steel* test, and therefore, we cannot say that its ruling was "clearly erroneous."

First, the Court heard testimony that the creditors who approved the plan believed that the rejection of the union contract was "highly involved" with the success of the plan. (Tr. 8) The Court itself noted that the testimony established that rejection would save the debtor some $100,000 per year. (Tr. 31) Therefore, the Court did have a basis upon which it could find that the collective bargaining agreement was burdensome to the debtor.

Second, the Court did weigh the equities in this matter. It noted that

> the union and the employees have a right to claim damages as a result of the rejection of the contract. They can file a complaint for the purpose of having damages fixed . . . and there will have to be a trial on the damages to ascertain what the damages will be.

(Tr. 32)

The transcript of the hearing in this matter reveals that the Court found that the collective bargaining agreement was burdensome to the debtor, and that it would be to his distinct advantage to reject the agreement. Furtheremore, the Court found that although the union and the employees would suffer injury as a result of the rejection, given their right to seek damages, the injury which they would suffer would not outweigh the advantage to the debtor from rejection.

Because we believe that there exists ample evidence in the record—and we note as the Bankruptcy Court did that the moving party's evidence was uncontradicted by the opposing side—to support the order below, we do not believe that any error was committed by the Bankruptcy Judge. Accordingly, the order will be affirmed.

The Court will enter an appropriate form of order.

APPENDIX D

Judgment of the United States District Court for the District of New Jersey

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF NEW JERSEY

Civil Action No. 81-513

IN THE MATTER OF:

BILDISCO, A General Partnership of the State of New Jersey,

Debtor

ORDER AFFIRMING JANUARY 15, 1981 ORDER OF BANKRUPTCY COURT

This matter being brought before the Court on appeal from an order granting the motion of the Debtor in Possession, Bildisco, to reject the Executory Contract dated May 1, 1979 with Teamsters Union Local No. 408 brought by Local 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen & Helpers of America, by Zazzali, Zazzali & Kroll, P.A., Albert G. Kroll, Esquire, appearing; and Ravin, Katchen & Greenberg, P.A., counsel for Bildisco, Jack M. Zackin, Esquire, appearing; and the Court, having considered the arguments of counsel and the papers submitted; it is on this 5th day of May, 1981.

Appendix D

ORDERED that the order entered in this matter on January 15, 1981, granting the motion of the debtor in possession to reject the Executory Contract be and hereby is affirmed.

ANNE E. THOMPSON, U.S.D.J.

Original Fled

May 6, 1981

ANGELO W. LOCASCIO, Clerk